gauge how interest rate fluctuations on mortgage securities affect your institution's capital and earnings. You may conduct the stress tests as described in either paragraph (a) or (b) of this section.

(a) Mortgage securities must comply with the following three tests at the time of purchase and each following quarter:

(1) *Average Life Test.* The expected WAL of the instrument does not exceed 5 years.

(2) *Average Life Sensitivity Test.* The expected WAL does not extend for more than 2 years, assuming an immediate and sustained parallel shift in the yield curve of plus 300 basis points, nor shorten for more than 3 years, assuming an immediate and sustained parallel shift in the yield curve of minus 300 basis points.

(3) *Price Sensitivity Test.* The estimated change in price is not more than thirteen (13) percent due to an immediate and sustained parallel shift in the yield curve of plus or minus 300 basis points.

(4) *Exemption.* A floating rate mortgage security is subject only to the price sensitivity test in paragraph (a)(3) of this section if at the time of purchase and each quarter thereafter it bears a rate of interest that is below its contractual cap.

(b) You may use an alternative stress test to evaluate the price sensitivity of your mortgage securities. An alternative stress test must be able to measure the price sensitivity of mortgage instruments over different interest rate/yield curve scenarios. The methodology that you use to analyze mortgage securities must be appropriate for the complexity of the instrument's structure and cashflows. Prior to purchase and each quarter thereafter, you must use the stress test to determine that the risk in the mortgage security is within the risk limits of your board's investment policies. The stress test must enable you to determine at the time of purchase and each subsequent quarter that the mortgage security does not expose your capital or earnings to excessive risks.

(c) You must rely on verifiable information to support all your assumptions, including prepayment and interest rate volatility assumptions, when you apply the stress tests in either paragraph (a) or (b) of this section. You must document the basis for all assumptions that you use to evaluate the security and its underlying mortgages. You must also document all subsequent changes in your assumptions. If at any time after purchase, a mortgage security no longer complies with requirements in this section, you must divest it in accordance with § 615.5143.

[64 FR 28899, May 28, 1999]

EFFECTIVE DATE NOTE: At 77 FR 66374, Nov. 5, 2012, § 615.5141 was removed, effective 30 days after publication in the FEDERAL REGISTER during which either or both Houses of Congress are in session.

§ 615.5142 Association investments.

An association may hold eligible investments listed in § 615.5140, with the approval of its funding bank, for the purposes of reducing interest rate risk and managing surplus short-term funds. Each bank must review annually the investment portfolio of every association that it funds.

[64 FR 28899, May 28, 1999]

§ 615.5143 Disposal of ineligible investments.

You must dispose of an ineligible investment within 6 months unless we approve, in writing, a plan that authorizes you to divest the instrument over a longer period of time. An acceptable divestiture plan must require you to dispose of the ineligible investment as quickly as possible without substantial financial loss. Until you actually dispose of the ineligible investment, the managers of your investment portfolio must report at least quarterly to your board of directors about the status and performance of the ineligible instrument, the reasons why it remains ineligible, and the managers' progress in disposing of the investment.

[64 FR 28899, May 28, 1999]

EFFECTIVE DATE NOTE: At 77 FR 66374, Nov. 5, 2012, § 615.5143 was revised, effective 30 days after publication in the FEDERAL REGISTER during which either or both Houses of Congress are in session. For the convenience of the user, the revised text is set forth as follows: